$50.00 ANNUALLY
40 Letters Per Year

DOW THEORY LETTERS, INC.

"The Market as Interpreted under the Dow Theory"

RICHARD RUSSELL
P. O. Box 15196
San Diego 15, California

Registered with the Securities and Exchange Commission

All Rights Reserved

THE MARKET The last confirmed highs of the 1962-63 rise were recorded by the Averages on August 30, 1963 (see Chart #1). Following the August 30 Rail peak of 176.86, the carriers headed down while Industrials pushed on to successive new highs. This unhealthy "parting of the ways" was further aggravated by the full divergence which developed between the advance-decline ratio and the Industrial Average, a divergence which began on September 5. The technical condition of the market has thus been weakening all during the months of September, October and November. This dangerous situation has been repeatedly pointed out to readers of these Letters.

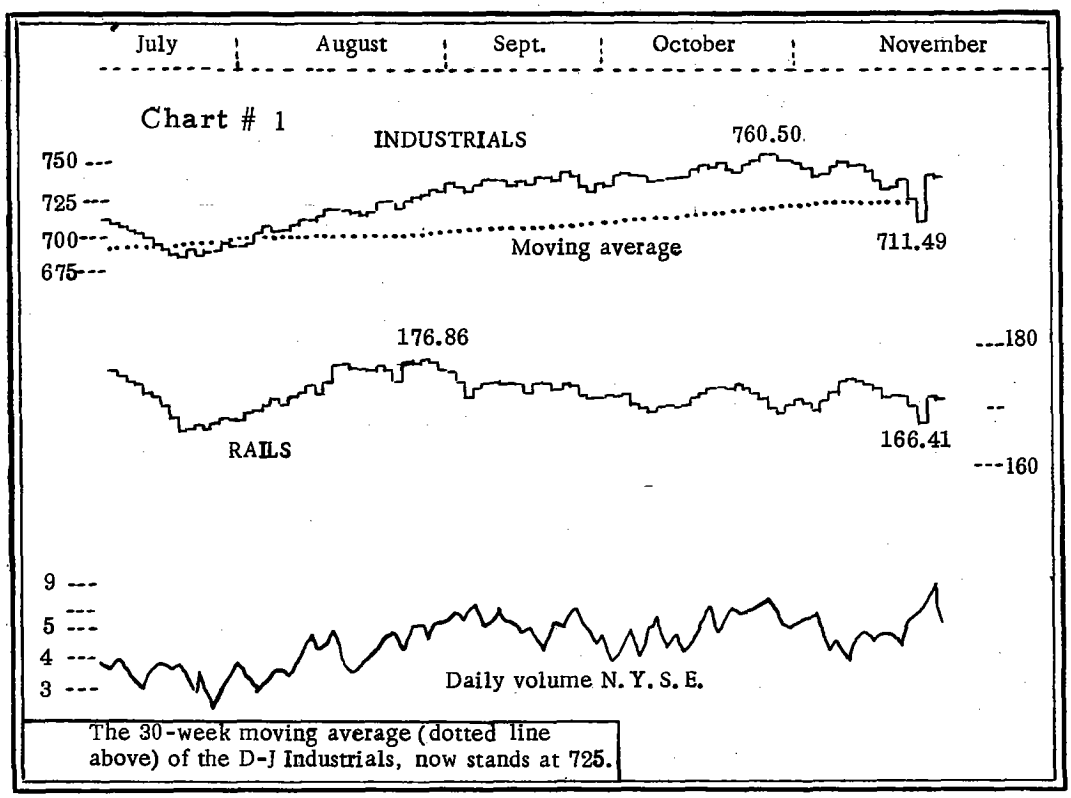
On November 21 (following a three-week decline), Industrials dropped 9.41 points while Rails sank 1.61 points. The Wall Street Journal described the move as "the sharpest break in more than a year". The deteriorating condition of the market which had been developing for months finally began making itself apparent in the actual price structure. On November 22 the market attempted to rally, but around mid-day the shocking news of the attack upon President Kennedy was announced. The market responded as it usually does to the unexpected -- it headed lower. An hour later the actual word of the President's death came over the wires, and the market became disorganized. Trading in many issues was suspended, and a few minutes later the market was officially closed. So ended Friday, November 22, 1963.

I had a chance to study charts of hundreds of stocks over the weekend. The damage which had been meted out to individual stocks was severe, and in a large number of instances, the action of Friday, November 22, was comparable to the worst day of the 1962 crash. Many stocks had dropped 10 to 25% during the single day of November 22; moreover, these collapses had occurred in stocks which had already developed well-established bearish trends. It was obvious that the panic had set off extraordinary "downward compression" in a market which was already technically weak. The result was an automatic recovery of the type which has followed every panic in recorded history.

The action following panic declines is one of the most consistent of all market movements. Hamilton's description (written in 1906) should serve as a guide: "It is a uniform experience, over the years when such records have been kept, that a panic decline is followed by a sharp rally of from 40 to 60 percent of the movement, and then by an irregular sag ultimately carrying the price to about the old low point"

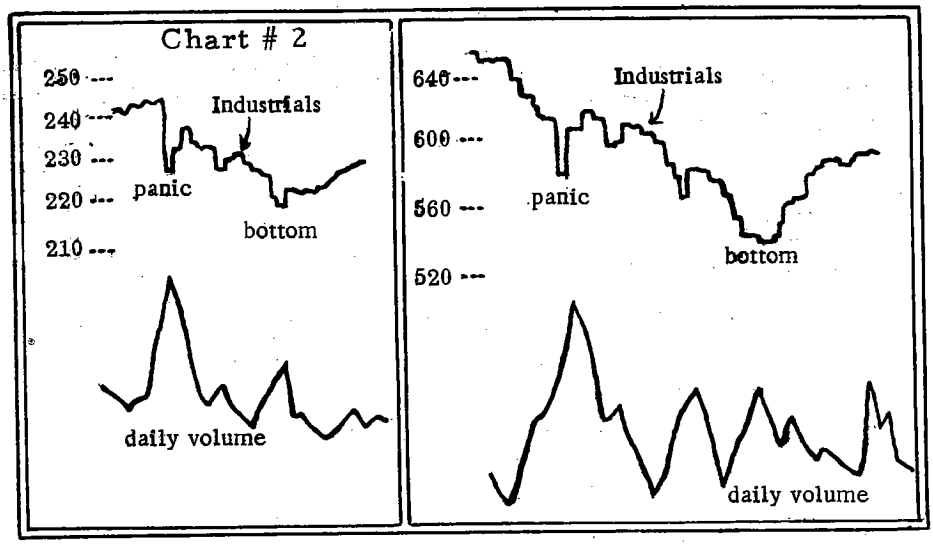
This writer has noticed that more often than not, following the initial automatic retracement of the panic drop, the second slower decline carries below the original panic low. This is what occurred following the panics of 1929, 1937, 1946, the Eisenhower heart-attack panic of 1955 and the (crash) panic of 1962. For purposes of illustration, I have included Chart # 2 (page 2) which shows two recent panics, the Eisenhower panic of 1955 (which was caused by news) and the 1962 panic (which was caused by a technical situation within the market itself). In each case, the result was essentially the same.

Note on Chart #2 that the first panic lows took place on very high volume (approximately 9 million shares in 1955, 14 million in 1962). In both cases two-day rallies came after the panic day, followed by a renewed decline, which within a matter of



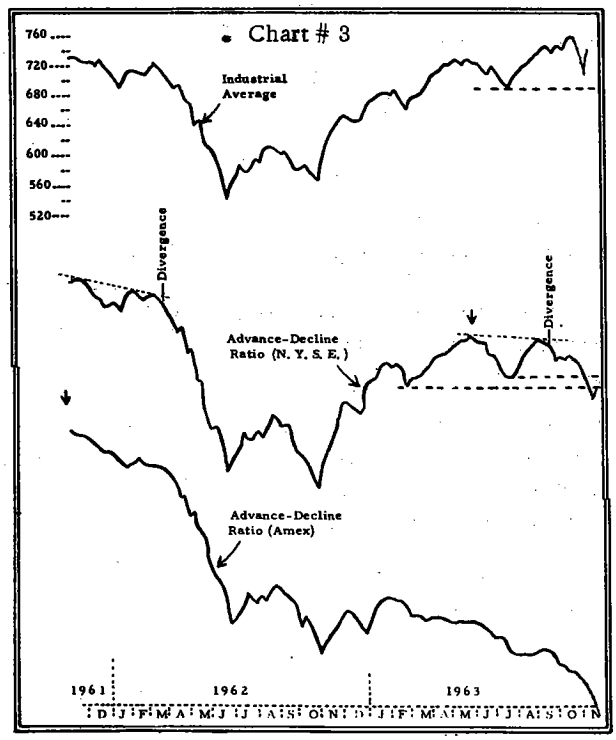
The 30-week moving average (dotted line above) of the D-J Industrials, now stands at 725.

weeks, succeeded in taking Industrials below their first high-volume low.



The action following the announcement of President Kennedy's assasination must be considered panic action as far as the price movement in the Averages and in individual stocks is concerned. The Exchange closed at 2:10 p. m. on November 22 with the tape twenty minutes late, and we do not know how huge the volume would have been had the Exchange decided to remain open. As a guess, I would estimate that we would have seen ten million or more shares.

The big question -- will the panic of November 22 be followed (in time) by the usual decline to or below the first panic lows, or has the market now embarked on an important new advance? My guess is that the Industrial Average will decline and perhaps approach or penetrate its November 22 low of 711.49. At least the odds, based on past history, favor such action. I might add that the only time I have ever seen a market go into a panic, then rise persistently from the first panic lows was last year (October, 1962) following the Cuban scare. That market was technically "soldout", however, and the Cuban crisis struck a market that was essentially still recovering from the worst spring collapse in market annals.



So much for the panic. A second amazing phenomenon is illustrated in Chart # 3. Here we see the materialization of a technical possibility which I have alluded to in many recent Letters. This is the breaking of the July low by the A-D ratio unconfirmed by the Industrial Average.

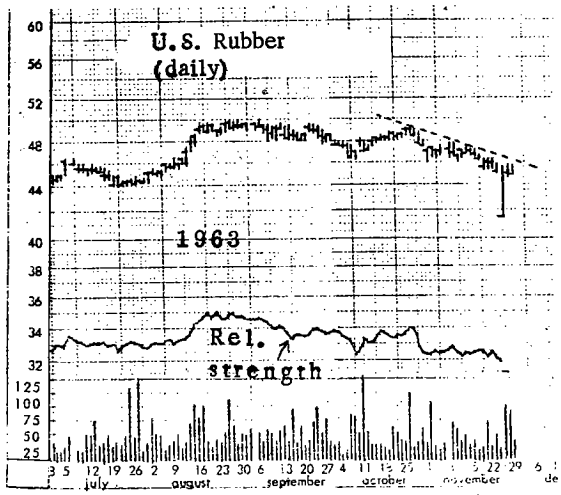
On November 21 the A-D ratio broke below its July low. On the panic day of November 22 the A-D ratio dropped substantially further -- actually sinking below its March, 1963, low. Neither of these penetrations was confirmed by Industrials (Industrials would have had to plunge under 687.71 to break their own July low). Thus the senior Average has continued to resist the broad decline which has affected the great majority of stocks on the N. Y. S. E. Such action allows for an important rally, and particularly for a rally in that one segment of the market which has stubbornly resisted the decline, the Industrial Average itself.

Technically, then, we have a picture as follows: a market which had been deteriorating for some months was suddenly struck by shattering news. During the course of a single day, stocks were forced to bearish extremes which might ordinarily have taken another month or so to produce. On top of this, the Industrial Average refused to confirm a penetration by the A-D ratio below its last important (July) low. The result was the technical formula for an important rally.

The problem -- did November 22 mark the beginning of the expected rally, or have we not yet seen the lows from which the next important rally will begin? On November 26, Industrials surged a monumental 32.03 points, Rails climbed 4.35 points, and volume soared to 9.3 million shares. Many were convinced that a major turn to the upside was underway. Despite the huge average gains, however, I noted that the A-D ratio did not gain nearly as much on the November 26 rise as it had lost on the November 22 panic. Moreover, daily new highs on November 26 dropped to a paltry 4 (against 7 on November 22), but more surprising new lows on November 26 registered a rather large 66.

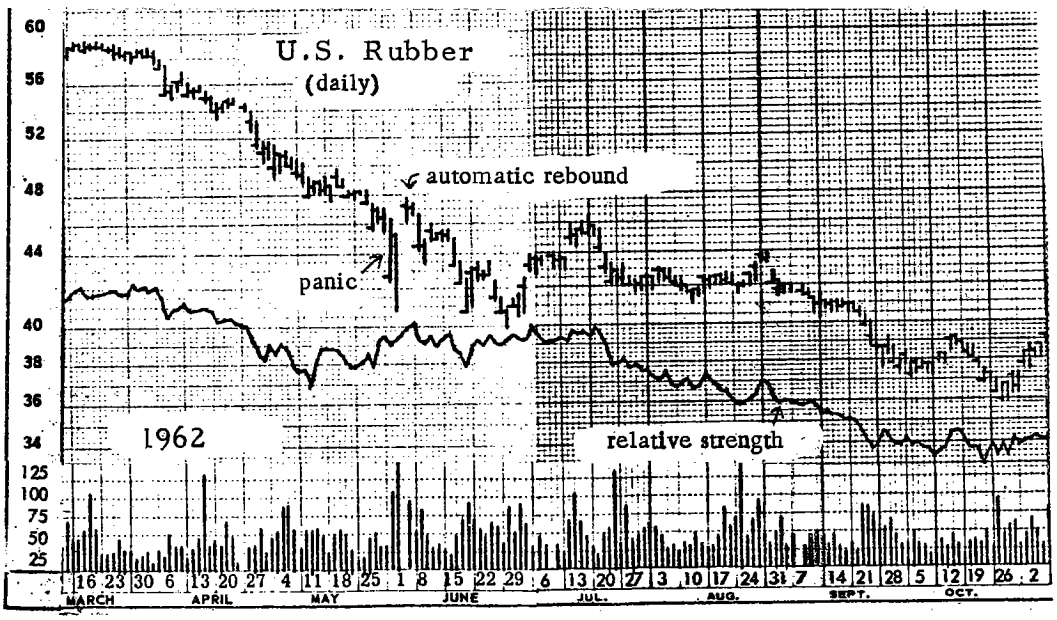
A few other remarkable facets of the November 26 action should be covered. First, the odd-lot public on November 26 purchased 10 shares for every 6 sold. This was not too abnormal, but it came following a few previous days of buying, and the result (taken all together) suggested that the public was beginning to view the whole market as "a buy". The 10-day average of odd-lot trading dropped on November 26 to its lowest selling rate of the year (although still remaining on the selling side). Nevertheless, a change in public sentiment appeared to be in the making. Normally, important low points in the market are delineated by a trend of less buying or more selling. The opposite appears to be the case at this time -- and this would favor lower prices.

The next point: after "panic" declines in many stocks on November 22, these same issues opened on November 26 at about their November 21 prices -- as if the panic had never occurred. This meant that there were few "bargain prices" on November 26, and those who bought stocks on that day were buying near the extreme highs -- not on or near the panic lows. Furthermore, most stocks, once having opened, did not make any appreciable progress during the day. Thus, buyers on the November 26 recovery found themselves in the position of owning stocks at prices far above the panic lows. Furthermore, in many cases these same stocks closed the day of November 26 below their opening prices. This meant that buyers on November 26 had paid fantastic recovery prices for stocks which might "lock them in" at losses, unless the market continued to tack on recovery gains on top of the 32 point (D. J. Industrials) gain of November 26. Veteran market practitioners do not like to purchase stocks on huge opening "leaps" -- just as they do not like to sell stocks on the bottom of panic declines. All of this made me wonder about the quality of the post-panic buying.

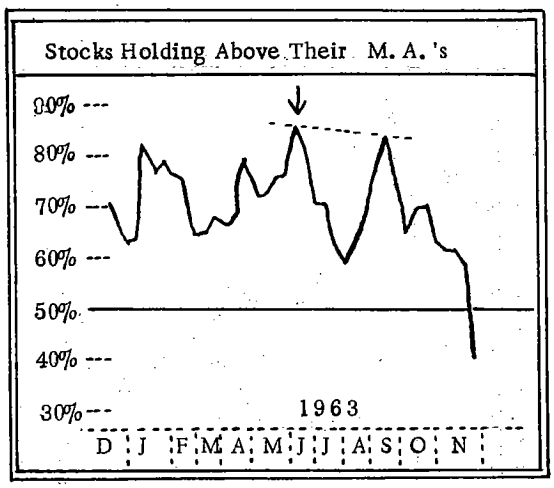


* * * * *

I feel that the following comparison should be of aid to readers. I have included two charts of a typical stock, U. S. Rubber. The larger chart shows the 1962 crash action and its aftermath. Note the May 1962, panic in Rubber, the explosive recovery on a "gap" opening, and then the normal steady decline to (in this case below) the original panic low. A second recovery began in late June, and this was followed by a July-October slump to a final low. The panic action of May and June is what I would like readers to study, as this is typical of the type of movement one may expect after the extraordinary "wound" caused by a panic drop in the market.

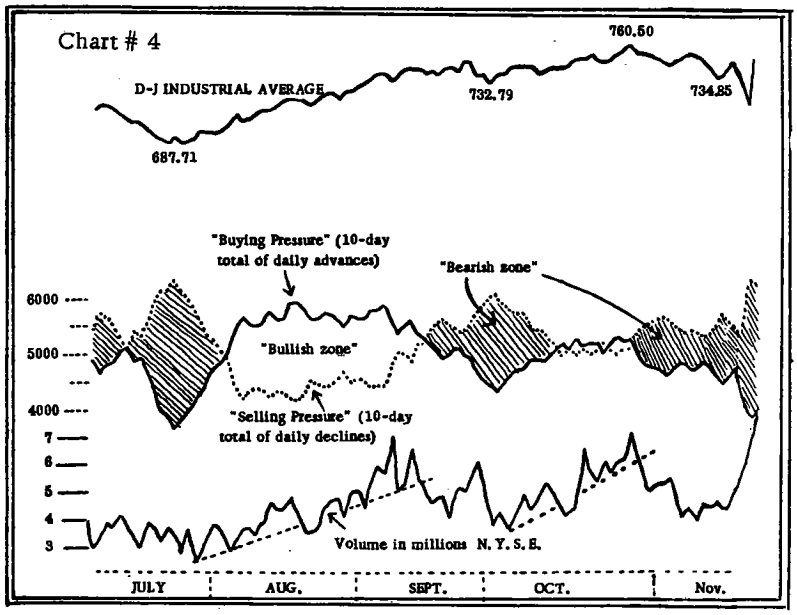


The smaller chart shows U. S. Rubber's action over the past few months, including the panic day of November 22 and thereafter. I would say that this chart is typical of most of the active stocks on the N. Y. S. E. during and following the November 22 panic. Note that Rubber had been in a definite downtrend. The downtrend began in August and became more pronounced during October and November. The panic day drove Rubber's price below all recent lows, and this high-grade equity lost over 10% of its market value in that single day! The recovery of November 26 put the stock right back in its downward channel -- almost as if the panic day had never occurred. Typically, Rubber opened on November 26 up 4 points, but it never got above its opening price. Those who bought the stock on November 26 purchased it on the high of the initial recovery.



MOVING AVERAGES Of 432 stocks tabulated here each week, 170 or 39% were holding above their 200-day moving averages as of Monday, November 25. This figure was taken before Tuesday's rebound. The chart at the bottom of the page shows the drop of the percentage indicator below the crucial 50% level. This is the first time that the percentage has declined under 50% this year. Such action may be taken as an important warning as far as the general market is concerned.

BUYING AND SELLING PRESSURE (See Chart #4) On November 22 Selling Pressure rose to the highest level of the year although Buying held above the July low. It is impossible at this time to say whether this represented the peak of selling. However, a steady downward trend in the Selling line accompanied by a steady rising trend in Buying will suggest that the worst has been seen as far as downward compression is concerned. If renewed selling is to enter the market, these lines should flare out again with Selling going to new highs and Buying to new lows. Such indications, however, will take time if they are to occur.



STOCKS I would expect the Industrial Average to retain its "stronger-than-the-market" characteristics during any further rally. Perhaps ironically (and it is unfortunate for traders), the strongest stocks in the Industrial Average are the higher priced issues. These consist of DuPont, Union Carbide, Telephone, Sears and Owens-Illinois Glass. These are the issues which I would expect to "tack on the yardage" if the senior Average rallies from here.

Three stocks (all discussed recently) continue to act better than the market: Sperry Rand, Paramount Pictures, General Tel. Aerospace issues (after a very poor two years) are beginning to act better than the market. United Aircraft (below) has pushed out of a one-year downtrend in both price and relative strength. It could be a leader on a rally. Minn. Mining (below) is a forgotten favorite. After dropping in rel. strength for three years, it appears to be gaining in popularity again. A large ascending triangle has been broken on the upside. MMM could also be a leader on any rally.

LATE NOTES As this is written, Industrials are still within 20 points or so of their all-time high. If the two Averages now push above their November 26 highs of 743.52 and 170.80 on increasing volume, it will probably mark the beginning of a year-end rally. Personally, I would not buy if the rally were to start from here. But if the Averages decide to approach or "test" the panic lows, the case for trading purchases will make considerably more sense. In the latter event, the first upward zig-zag from the lows (in both Averages) will probably identify the turn to the upside. (If we do approach the panic lows, however, we will have time to think and act). Written Friday, November 29, noon N.Y. time.

* * * * *

Tabulations (page 3) of bullish percentage of the 432 stocks from Quote Digest, 110 North Lorraine, Wichita, Kansas. Chart of MMM and United Aircraft courtesy of Traders Research, 1431 Pearl Avenue, Alton, Illinois 62003.